Key possibility to ensure efficient investment fund distribution and simple investor journeys

The fight against money laundering and terrorist financing is crucial and requires strong and targeted regulation. A comprehensive scope is therefore necessary for the regulation to encompass all possible risks. Nonetheless, in keeping with the overarching political focus on simplification and creating a strong Savings and Investments Union (SIU) in the EU, the regulation must be targeted using a risk-based approach. Harmonization of regulation at the EU level is fundamentally supportable and promotes the functionality and competitiveness of European internal markets as a whole. However, the new AMLR provides a general rulebook which has not sufficiently taken into account the regulation's impact on the fund industry, particularly in the Nordics. The AMLR creates uncertainty as to how to define customer relationships in regard to the fund industry – i.e. if an investor (unit holder in a fund) is both considered a customer of the fund itself and of the financial intermediary through which the investor has made their investment[1]*. This seems to entail that all asset managers (i.e. collective investment undertakings, cf. art. 2(1)(6)(e) of AMLR) will be obliged to perform customer due diligence (CDD) for all investors in their products, without consideration for how CDD information should be obtained within an operationally variable model for asset managers, and without regard for how these requirements affect the investor journey.* ***If not amended or exempted through delegated regulation, this will have comprehensive and detrimental effects for EU capital markets, investor participation, simplification, and for the competitiveness of EU asset managers.***

Consequences for EU agendas

If not solved, the requirement for asset managers to conduct CDD in spite of having no business relationship to investors will negatively impact a number of key EU agendas:

- Simplification
- Increasing retail investor participation and a simple investor journey
- Promotion of Savings & Investment Accounts
- Ensuring democratic access to investment products
- Competitiveness of EU capital markets and EU asset managers

Impacts of AMLR on fund distribution – with no business relationship between investors and asset managers

AMLR applies to asset managers who distribute their products through other financial intermediaries, such as banks, investment platforms, etc., which accounts for the vast majority of the market. Obliged entities under AMLR must perform CDD on their business relationships, however, it is unclear whether investors in a fund are considered to have a business relationship with the fund itself. If that is the case, the asset manager must know the customer and accept them as a customer, as well as their risk profile, before fund subscription. In accordance with art. 18 of AMLR, some of the applicable obligations may be outsourced, but not all.

[1] The uncertainty regarding the definition of customer relationship is not clarified in section 16.14 of the existing EBA Guidelines on Risk Factors (EBA/GL/2021/02), as the guidelines imply that the asset manager would hold their own unitholder register which is not always the case.

Most often, investors invest through their bank or investment platform, who are distributors of the investment products. That entails that the asset manager in such cases has no direct contact with the end investor – i.e. there ought not to be business relationship between the asset manager and the investor, as in accordance with AMLR art. 2(1)(19). Rather, the business relationship exists between the asset manager and the distributor of the product – if there is a distribution agreement between the two – and between the distributor and the investor. When investing through a bank, investors are required to maintain custody or fund account, and they are therefore subject to CDD prior to being able to invest. As a result, the risks associated with money laundering and terrorist financing are substantially mitigated, as the distributor is rightfully obliged to conduct CDD procedures on their customers. The asset manager has no complete information on the investors holding their products distributed through external distributors. If the asset manager were to conduct CDD procedures on the investors, it would require substantial new information sharing and record-keeping arrangements between investors, distributors, and asset managers – which adds comprehensive GDPR-obligations. This results in the need for highly complex new resources as well as a more complicated and lengthy investment process for investors. The impacts on the investor journey can lead to unfinalized transactions and result in lower retail participation in the Nordic financial markets. Asset managers would need to obtain accurate information from distributors on any investors in their products, and this information would need to be updated very frequently to reflect changes in existing investors' holdings, new investors, and investors exiting their positions. In many cases, this is not operationally possible due to the nature of fund distribution.

If asset managers must perform CDD under AMLR, when there is no contact with the end investor, it will have detrimental consequences particularly for Nordic markets and for the competitiveness of Nordic funds due to the specificities of the fund distribution models in the Nordics. Ultimately, it may even hinder distribution and cause a decline in the product offering for investors contrary to the objectives of the SIU, also due to restrictions on the extent to which these services may be outsourced under art. 18 of AMLR:

- **Listed funds traded on a common fund exchange (Sweden and Denmark)**
  In Sweden and Denmark, many funds are traded on a common fund exchange (similar to a regular stock exchange). One of the features of the Danish and Swedish fund markets is that funds are marketed from a wide range of distributors. They in turn market a wide range of funds from different asset managers and are acting independently from the asset management companies. This has proven very beneficial for retail investors. The marketing of funds through these distributors is structured in the same way as stock trading. This means that it is the full responsibility of the distributor to conduct CDD. There is no business relationship between the asset manager and the customers of the distributor. Instead, the distributor – acting in its own name – is the customer of the asset manager. Asset managers routinely verify and monitor that the distributor, in turn, has the necessary procedures in place to prevent money laundering and the financing of terrorism.

  In the context of open markets and markets that operate with non-nominee account structures due to regulatory or market infrastructure related reasons (as in Finland)), introducing direct CDD obliga-

tions for asset managers could also have negative consequences for investor protection. If the completion of a CDD process is required before the investor can make their investment, it will make the process longer. When funds are listed or traded through multiple distributors, a longer investment process could therefore result in the investor missing out on beneficial pricing points (when the fund's Net Asset Value is set), forcing the transaction to be made later at a potentially less favorable price. This undermines the principle of fair and timely access to investment products and may disproportionately affect retail investors who rely on streamlined access through distributors.

- **Protecting client registers as a commercial asset (Sweden, Norway, and Denmark)**
  The CDD obligations are described further in the proposed draft RTS art. 21 set forth by EBA[2]. EBA has interpreted the regulation in a way that brings investment firms and asset managers within the scope of art. 20(1)(h) of the AMLR, which seemingly was not the intention of the legislator. The RTS outlines a simplified due diligence process when there is no direct client contact; however, this is currently unclear and, to some extent, not operational in practice. The proposal in draft art. 21 would furthermore damage the Swedish, Norwegian, and Danish models for fund distribution by obliging asset managers to obtain CDD information from independent distributors. In Sweden, Norway, and Denmark, distributors – licensed investment firms and credit institutions – act in their own name and hold their own client registers, which represent one of their most valuable commercial assets. Requiring them to disclose this information to asset managers, who are often direct competitors with their own distribution channels, would be highly commercially sensitive and practically unworkable. Such a measure would not enhance money laundering prevention but would instead dismantle a well-functioning and competitive market structure. Please see the attached annex containing a detailed consultation response regarding the draft RTS from the Swedish Investment Fund Association.

- **Register of investors in unitholder registers and outsourcing (Finland, Iceland and Denmark)**
  Both Finnish and Danish fund industries operate in a model where the end investor is directly registered in the unitholder register. This deviates from the standard European distribution model. As described above, AMLR creates uncertainty as to whose customer the unitholder (investor) is, and it could therefore be implied that asset managers should perform CDD for all investors registered in the unitholder register in relation to their products.

  In markets where units of funds are primarily not held under nominees i.e. in beneficial owner accounts, as is the case in Denmark and Iceland where units are registered in the local CSD, or directly in the name of the beneficial owner in the unitholder register, as in Finland[3], the interpretation of who the asset manager's customer is from an AML perspective is of utmost importance. As not all CDD-related obligations may be outsourced, it is essential that the definition of an asset manager's customers is clear and accurately set. For instance, in the Finnish model, the bank or investment services company

[2] Draft RTS under art. 28(1) of AMLR.

[3] Finnish fund regulation contains national regulation that deviates from general European fund regulation in the form of a prohibition on nominee registration.

acting as distributor has an independent obligation to perform CDD as well as better prerequisites than asset managers to assess risk factors related to the customer. The asset manager has no direct connection to unitholders nor often even real-time visibility to the unitholder register, since distributors maintain information in their own systems.

Therefore, to secure the competitiveness of funds operating in these so-called non-nominee markets, it must as a minimum be clarified that where maintenance of the unitholder register is outsourced to e.g. a CSD or distributor and the asset manager is not in direct contact with the unitholder, the unitholder is exclusively the customer of account operator in the CSD or the distributor, who has sold the product to the customer. To require CDD on all unitholders from the asset managers and further to restrict the opportunities to outsource the related tasks under art. 18 of the AMLR introduces a disproportionate compliance burden with no clear reduction in risk.

The extensive distribution of funds also in the future requires as a minimum that the scope of application of the exception concerning art. 18(7) of AMLR is clarified so that the asset management company can outsource the tasks referred to in art. 18(3)(c), (d) and (e) when the maintenance of the fund unit register has been outsourced to a distributor or delegated to a CSD. Regardless, we want to highlight that the prohibition to outsource tasks referred to in art. 18(3)(f), i.e. approval of the criteria for the detection of suspicious or unusual transactions and activities, may in practice become a barrier to using distributors outside the same group, as this type of information is highly sensitive and is not typically shared with other companies.

Against this backdrop, the regulatory objective of the proposed AMLR appears misaligned with the principles of a risk-based approach. As imposing an additional obligation on asset managers, who have no direct contact with the end investors, to conduct CDD on investors introduces a disproportionate compliance burden, where the cost significantly outweighs any incremental reduction in risk.

If not resolved, Nordic markets will be heavily affected. It will generally threaten the open architecture of fund markets and the listed markets for funds in particular. The open architecture in the Nordics supported by exchanges is one of the key drivers for a competitive and well-functioning retail fund market in the region. Ultimately, the negative effects on the fund markets will harm investment fund distribution, the investor journey, investor protection, and investor participation.

Possible solution

Under AMLR art. 3(2), asset managers are included as an obliged entity, and CDD requirements apply when an obliged entity has business relationships. The AMLR does not contain a definition of whose customer the unitholder is. As described above, asset managers – in most cases, representing the majority of the market – do not have business relationships with the investors. The business relationship is between the distributor and the customer. If this interpretation is acknowledged by the legislator, it would significantly address the serious challenges outlined above.

In this case, however, **for a harmonized approach and legal clarity, it must be made explicit that the legislator interprets the rules to mean that in all cases where asset managers do not have direct client contact, no CDD requirements apply**.

Nevertheless, if such an interpretation is not correct, it should be clarified and reinforced in the draft RTS 28(1)(b) on CDD to ensure that the purpose of art. 21 is broadened – namely, to prevent the negative market impact described above when the AML package enters into force in July 2027.
The simplified CDD approach outlined in art. 21 should be sufficiently flexible and comprehensive to accommodate the current structure and functioning of the investment fund distribution market, ensuring that CDD procedures do not impose constraints that would hinder the market from operating as it does today.